Office - Supreme Court, U. S.
FILED
SEP 23 1955
HAROLD B. WILLEY, Clerk

No. 51

In the Supreme Court of the United States

OCTOBER TERM, 1955

FEDERAL POWER COMMISSION, PETITIONER

v.

SIERRA PACIFIC POWER COMPANY

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR THE FEDERAL POWER COMMISSION

SIMON E. SOBELOFF,
Solicitor General,
WARREN E. BURGER,
Assistant Attorney General,
MELVIN RICHTER,
LIONEL KESTENBAUM,
Attorneys,
Department of Justice,
Washington 25, D. C.

WILLARD W. GATCHELL,
General Counsel,
HOWARD E. WAHRENBROCK,
Assistant General Counsel,
WILLIAM J. GROVE,
Assistant General Counsel,
DREXEL D. JOURNEY,
Attorney,
Federal Power Commission,
Washington 25, D. C.

INDEX

	Page
Opinions below	1
Jurisdiction	1
Question presented	2
Statute involved	2
Statement	2
Summary of Argument	10
Argument	13
I. The Commission properly applied the filed rate procedure set out in Sections 205(d) and 205(e) of the Power Act to the new schedule filed by the Public Utility, even though the existing rate was embodied in a contract	13
A. The Commission's application of Sections 205(d) and 205(e) accords with the terms of the Power Act and the usual provisions of utility regulatory statutes	13
B. The application of the filed rate procedure does not result in inequity to Sierra	19
II. The Commission's determination that the proposed rate filed by the Public Utility was reasonable is supported by substantial evidence	21
A. Applying appropriate standards for fixing rates, the Commission properly found that the proposed rate will provide no more than a fair return to the Public Utility from its service to Sierra and is therefore reasonable	23
B. The Commission was not required to depart from the established rate-making standards by Sierra's claim of special circumstances surrounding negotiation of the 1948 contract rate	27
1. Existence of a contract does not alter the test of reasonableness	28
2. The facts, as found by the Commission, did not justify departure from the cost of service test	29
3. Sierra seeks favored treatment	35
Conclusion	38
Appendix	39

CITATIONS

Cases:

	Page
Armour Packing Co. v. United States, 209 U.S. 56	18
B. & O. R.R. Co. v. United States, 345 U.S. 146	29
Banton v. Belt Line Ry., 268 U.S. 413	26
Cities Service Gas Co. v. Federal Power Commission, 155 F. 2d 694, certiorari denied, 329 U.S. 773	26
Colorado Interstate Gas Co. v. Federal Power Commission, 324 U.S. 581	26
Duquesne Light Co. v. Public Service Commission, 273 Pa. 287	28-29
Federal Power Commission v. Hope Natural Gas Co., 320 U.S. 591	26, 27, 29
Federal Power Commission v. Mobile Gas Service Corp., No. 31, this Term	1
Federal Power Commission v. Natural Gas Pipeline Co., 315 U.S. 575	27
Harrison Electric Co. v. Citizens' Ice & Storage Co., 147 Ark. 502	18
Hope Natural Gas Co. v. Federal Power Commission, 196 F. 2d 803	19, 20
Interstate Commerce Commission v. Chicago Great Western Ry., 209 U.S. 108	26
Menasha W. W. Co. v. Minneapolis, St. P. & S.S.M. Co., 245 U.S. 633, affirming 159 Wisc. 130	18
Midland Realty Co. v. Kansas City Power & Light Co., 300 U.S. 109, affirming 338 Mo. 1141	16, 18
Mobile Gas Service Corp. v. Federal Power Commission, 215 F. 2d 883, pending on writs of certiorari Nos. 17, 31, this Term	9, 10, 14, 15, 16, 18, 19, 22
Montana-Dakota Utilities Co. v. Northwestern Public Service Co., 341 U.S. 246	22, 26
Northern Pacific Ry. v. North Dakota, 236 U.S. 585	26
Pacific Gas and Electric Company v. Sierra Pacific Power Company, No. 53, this Term	1
Panhandle Eastern Pipe Line Co. v. Federal Power Commission, 324 U.S. 635	26
Pennsylvania Water & Power Co. v. Federal Power Commission, 193 F. 2d 230, affirmed 343 U.S. 414	26
Public Service Commission v. Pavilion Natural Gas Co., 232 N.Y. 146	18

Cases, Continued

	Page
Safe Harbor Water Power Corp. v. Federal Power Commission, 179 F. 2d 179, certiorari denied, 339 U.S. 955	26
Suburban Water Co. v. Oakmont Borough, 268 Pa. 243	18
United Gas Pipe Line Co. v. Mobile Gas Service Corp., No. 17, this Term	4
United States v. Public Utilities Commission of California, 345 U.S. 295	36
Universal Camera Corp. v. National Labor Relations Board, 340 U.S. 474	23
Wichita R.R. v. Public Utilities Commission, 260 U.S. 48	18

Statutes:

Federal Power Act, 49 Stat. 838, 16 U.S.C. 791a:	
Sec. 205	5, 6
Sec. 205(c)	39
Sec. 205(d)	4, 13, 16, 39
Sec. 205(e)	4, 13, 16, 20, 22, 23, 40
Sec. 206	5
Sec. 206(a)	9, 10, 15, 16, 21, 23, 41
Sec. 306	41
Natural Gas Act, 52 Stat. 821, 15 U.S.C. 717, *et seq.*:	
Sec. 4	6, 14
Sec. 4(d)	10
Sec. 4(e)	10, 20
Sec. 5	10
Sec. 5(a)	15
California Public Utilities Code:	
Sec. 454	36
Sec. 455	36

Miscellaneous:

18 C.F.R. 35.4-13	17
18 C.F.R. 35.3(c)(17)	4
H. Rep. No. 1318, 74th Cong., 1st Sess., p. 29	17
S. Rep. No. 621, 74th Cong., 1st Sess., p. 51	17

In the Supreme Court of the United States

OCTOBER TERM, 1955

No. 51

FEDERAL POWER COMMISSION, PETITIONER

v.

SIERRA PACIFIC POWER COMPANY[1]

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR THE FEDERAL POWER COMMISSION

OPINIONS BELOW

The opinion of the Court of Appeals (R. 478-482) is reported at 223 F. 2d 605. The opinions and order of the Federal Power Commission (R. 443-477) are reported at 7 PUR 3d 256.

JURISDICTION

The original judgment of the Court of Appeals was entered on February 24, 1955 (R. 483). Thereafter,

[1] This is a companion case to *Pacific Gas and Electric Company v. Sierra Pacific Power Company*, No. 53, this Term, also pending before this Court on a writ of certiorari. A related question under the Natural Gas Act is presented in *Federal Power Commission v. Mobile Gas Service Corporation*, No. 31, this Term, and its companion case, *United Gas Pipe Line Co. v. Mobile Gas Service Corporation*, No. 17, this Term.

on the motion of Sierra Pacific Power Company, the Court of Appeals modified its judgment on March 23, 1955 (R. 495). The petition for a writ of certiorari was filed on April 20, 1955 and granted on May 23, 1955 (R. 496), 349 U.S. 907. The jurisdiction of this Court rests on 28 U.S.C. 1254(1) and Section 313(b) of the Federal Power Act.

QUESTION PRESENTED

Whether, under the Federal Power Act, the Federal Power Commission may permit a schedule increasing a public utility's rate for the sale of electric energy for resale to be filed, become effective, and supersede the existing filed rate upon a finding after full hearing that the increased rate is not unlawful, but without a finding as to the unlawfulness of the existing rate, where the existing rate is embodied in a contract between the public utility and its purchaser filed with the Commission as a rate schedule, and the purchaser has not agreed to the increase.

STATUTE INVOLVED

The pertinent provisions of the Federal Power Act, 49 Stat. 838, 16 U.S.C. 791a, *et seq.*, are set out in the Appendix, *infra*, pp. 39-42.

STATEMENT

Respondent, Sierra Pacific Power Company, distributes electric power to customers in eastern California and northern and northwestern Nevada (R. 5, 467). It purchases 77% of its power requirements from Pacific Gas and Electric Company (PG&E), a "public utility" under Part II of the Federal Power Act (R. 466-7).

Sierra's purchases from PG&E began under contract in 1923 and continued under agreements entered

into in 1938 and 1948 (R. 6, 261, 443, tn. 1). The 1948 contract (R. 138-146) was negotiated before the expiration of the previous agreement in order to increase Sierra's capacity to meet a growing demand upon its system (R. 6-8, 232-233, 170-171, 199-200, 205-208, 231-232, 264). It provided for the construction of an additional 110 kv line (and, if necessary, a second such line) to supply the additional power (R. 142-144) and for the purchase of Sierra's requirements from PG&E until December 31, 1964, or fifteen years after the new lines went into service, whichever is later (R. 139, 145). Sierra agreed that it would purchase power exclusively from PG&E except for minor standby and exchange agreements (R. 139). The contract provided that charge for standby service and demand and energy charges for firm power service; the rate agreed upon was lower than PG&E's previous rate to Sierra (R. 139-140). This 1948 contract was filed with the Commission as PG&E's Rate Schedule FPC No. 3 (R. 428, 444).

Subsequently, on February 2, 1953, PG&E filed with the Commission the schedule here involved, designated as Supplement No. 1 to its Rate Schedule No. 3 (R. 428-430), increasing its rate to Sierra by about 28%, or by an estimated $119,400 for 1953 (R. 443).[2] The new schedule substituted increased demand and energy charges for those theretofore used in billing Sierra for the approximately 40,000 kw of firm power purchased

[2] The Commission found, without objection, that the sale was in interstate commerce for resale, within the Commission's regulatory jurisdiction (R. 448, 467-468). The only other PG&E services within the Commission's jurisdiction are its sales to California-Oregon Power Company (R. 456, 469). PG&E's other sales are in intrastate commerce and are subject to regulation by the California Public Utilities Commission (R. 457, 280-283, 411-413).

under the 1948 agreement; the other terms of the contract were to remain in full force and effect (R. 428-430, 444). PG&E requested that the new schedule be effective April 6, 1953 (R. 431, 444), thus giving more than the thirty days' notice of rate change required by Section 205(d) of the Federal Power Act, *infra*, p. 39.[4]

In response to the Commission's request for comments, Sierra objected to the increase as unreasonable and unjust and claimed that, although the 1948 contract rate might fail to provide a fair rate of return, it was just and reasonable because of the circumstances at the time the contract was made (R. 432).[5] Thereafter, on March 13, 1953, the Commission, stating that the increased rates "may be unjust, unreasonable, unduly discriminatory or preferential," entered upon a hearing "concerning the lawfulness of the proposed rates," as authorized by Section 205(e) of the Power Act, *infra*, pp. 40-41 (R. 433). In addition, pending the outcome of the hearing the Commission, acting under the further provisions of 205(e), suspended the proposed rates until September 6, 1953, five months after April 6, 1953, the effective day requested by PG&E

[3] The proposed charges and those to be superseded are similar to PG&E's schedules "R" and "P-31," respectively, filed with the California Public Utilities Commission. The former superseded the latter as the rate generally available for intrastate service to resale customers with no generating facilities of their own and purchasing only from PG&E (R. 2-4, 444 and fn. 2).

[4] Where a rate increase is proposed by the utility, the Commission regulations require the filing of certain data 60 days prior to the proposed effective date of the increase. 18 C.F.R. 35.3(c)(7).

[5] The California Public Utilities Commission refused to comment since a similar application filed by PG&E was then pending before it. The Nevada Public Service Commission opposed the increase because of the contractual arrangement between PG&E and Sierra and requested a hearing (R. 432, 435-437).

(R. 433-434). Subsequently, when the Commission was unable to reach its decision by September 6, the proposed increase became effective (R. 440). However, under the authority of Section 205(e), the Commission by further order directed PG&E to put into a special reserve the difference between its charges at the two rates, plus interest, subject to refund should the Commission find any portion of the increased rate to be unjustified (R. 440-442).

Meanwhile, Sierra petitioned for leave to intervene in the proceeding and also requested the Commission to reject the proposed schedule as improperly filed on the ground that contract rights may not be changed under the rate filing and suspension provisions of Section 205 of the Power Act (R. 145). The Commission permitted Sierra to intervene but denied the request that the schedule be rejected—without prejudice, however, to Sierra's right thereafter to press these contentions (R. 445-446).[6]

At the hearing, Sierra renewed its contentions that the proposed supplement should be rejected. It claimed that Section 205 does not authorize alteration of a contract by the "unilateral act" of a public utility in filing new rates, or by an order of the Commission entered in a proceeding held on the suspension of such filing. Rather, it urged that contracts may be altered only after a rate investigation under Section 206 of the Act, *infra*, p. 41, and upon a finding that the contract rate was unlawful; it also contended that such a finding as to the reasonableness of the existing contract rate was re-

---

[6] Sierra's petition for rehearing on this denial was dismissed because it related only to an interlocutory and procedural ruling, not a final decision by the Commission (R. 446).

quired before a schedule filed under Section 205(d) could be permitted to become effective (R. 458). In addition, it urged the Commission to find the 1948 contract rate reasonable and the proposed increase unreasonable. It claimed that the contract rate had been offered by PG&E in order to retain Sierra as a customer; that in reliance upon the binding effect of all terms of the 1948 agreement, Sierra had given up opportunities to meet its power requirements from other sources, notably from the United States Bureau of Reclamation; and, consequently, that to increase the rate and leave the other provisions of the 1948 contract unaltered would be grossly unfair (R. 450).

In its opinion and order, entered after hearing and oral argument followed by further hearing and argument, the Commission pointed out that "on each of the several previous occasions when we have been called upon to interpret the scope of Section 205 of the Power Act or the equivalent Section 4 of the Natural Gas Act, we have rejected any contention that an abrogation of contract rights may not be worked by the operation of the statutory rate filing and suspension provisions" (R. 458-459). Noting that "even a cursory examination will show that the provisions of Section 205 expressly authorize the alteration of contracts" (R. 461), the Commission went on to rule that the filed rate procedure provided in Section 205 imposed no requirement that the old contract rate must be found unlawful before a new rate can take effect (R. 462):

> * * * There is nothing in that section that qualifies or limits the right and duty placed upon the seller to maintain rates which satisfy the statu-

tory standard by any requirement for the consent of the buyer or for a Commission finding with respect to the former contract rate. The sole condition is that the filed rate may not become effective in less than 30 days (unless the Commission otherwise orders) and the Commission may suspend any filing and prescribe a rate in lieu thereof if, after hearing, it finds that the changed rate proposed by the suspended filing is unlawful.[7]

As to the reasonableness of the new rate, the Commission found that the rate would provide revenues sufficient to yield a return of 4.75% on a net investment rate base, less than the 5½% return which is generally reasonable for PG&E's electric utility operations (R. 448-449). Despite Sierra's contention that the rate of return was of no consequence here because of the circumstances under which (as Sierra claimed) the 1948 contract was agreed upon (R. 432, 450), the Commission refused to depart from its usual method of testing the reasonableness of rates against the cost of service (R. 450-455). It found "unconvincing" Sierra's claim that it had foregone other sources of supply in reliance upon the continuance of all terms of the 1948 agreement since "the record * * * clearly shows that in 1948 Sierra regarded the other sources of supply as being so unacceptable that PG&E became, in fact, the only feasible

[7] In this connection, the Commission noted that "if a finding on the lawfulness of the 1948 contract rate were necessary or appropriate, on the record before us that finding would have to be that the 1948 rate is unreasonably low and therefore unlawful" (R. 464). However, since the Commission regarded the question before it as relating only to the reasonableness of the proposed rates, it did not enter formal findings as to the reasonableness of the 1948 contract rate (R. 469-470).

source" (R. 451).[8] Relying on the principle that a public utility cannot by contract place its rates beyond the reach of regulation, the Commission also rejected Sierra's argument that the competitive aspects of the 1948 negotiations necessarily made the negotiated rate just and reasonable for the entire duration of the contract (R. 450-451). Finally, it noted that even if it accepted the rate of return then foreseeable under the 1948 contract as reasonable for Sierra's business, "due to the increases in other costs which have occurred since, then the presently proposed increase will merely restore that rate of return, not go above it" (R. 452).[9]

Consequently, since it was of the opinion that the proposed rate would not provide more than a fair return on the portion of PG&E's net investment rate base properly allocable to that service (R. 469),[10] the Com-

---

[8] In regard to Sierra's contention that it would be grossly unfair to change the 1948 rate and leave all other terms unaltered, the Commission said that "Sierra has not shown, and on cross examination its president could not suggest any alterations which he thought should be made in other terms if the rate were changed as proposed" (R. 451).

[9] To compare the rate of return which would result from the revenues produced by the new rate with the return reasonably foreseeable at the time the 1948 contract was negotiated, the Commission used computations made by PG&E and determined that there was no substantial difference between the reasonably foreseeable rates of return (R. 452-453). While the Commission did not accept (without certain adjustments) PG&E's method of computation as comprehensive for purposes of stating the return from the new rates, PG&E's result being too low, that method was sufficient basis for comparing the returns under the two schedules between themselves (R. 452-3). See *infra*, pp. 33-35.

[10] Although 5½% is generally a reasonable rate of return on PG&E's electric utility business, and the proposed rate would, under the Commission's computation, result in a 4.75% return, the Com-

mission concluded that the proposed rate was not unlawful and terminated the proceeding (R. 470).[11]

Sierra sought review of the Commission's order in the court below (R. 478-9). That court held that a contract rate on file with the Commission remains effective until it is found unreasonable by the Commission under Section 206(a), *infra*, p. 41; and such a rate cannot be increased by the selling utility's filing under Section 205 of a new rate, even though it is found to be reasonable by the Commission (R. 480-1). Since the Commission had not (so the court thought) found the 1948 contract rate to be unreasonable, the court set the order aside and remanded the case to the Commission with instructions to dismiss the proceeding entirely or for further proceedings in the same case under Section 206(a) (R. 482). In so holding, the court placed primary reliance upon the reasoning and the material cited, as well as the ruling, in *Mobile Gas Service Corporation* v. *Federal Power Commission*, 215 F. 2d 883 (C. A. 3) pending on writs of certiorari, Nos. 17, 31, this Term (R. 481-2). On March 23, 1955, the court modified its order by deleting the permission to continue the present case with further proceedings under Section 206(a) (R.

---

mission did not regard the 0.75% deficiency as a basis for rejecting the proposed rate in view of PG&E's willingness to absorb the deficiency, the ruling of the California Commission preventing a shift of such deficiency to other customers, and the fact that no undue discrimination or preference resulted (R. 464-465).

[11] Two Commissioners dissented on the ground that "the circumstances surrounding the origin and development of existing contractual relationships between PG&E and Sierra have been such as to justify—or in equity to require—special consideration" (R. 472) and the 1948 contract rate should be continued because not unjust, unreasonable, or unduly discriminatory (R. 471-477).

495), so that the Commission is now required to dismiss the case and start anew.[12]

SUMMARY OF ARGUMENT

I

A. The court below relied on *Mobile Gas Service Corp. v. Federal Power Commission*, 215 F. 2d 883, now pending on writs of certiorari, Nos. 17, 31, this Term, in holding that the Commission may not permit new schedules filed by a utility under the filed rate procedure of Sections 205(d) and 205(e) of the Power Act to supersede rates embodied in a contract, and instead must first pass on the reasonableness of the existing contract rate under the complaint-hearing procedure of Section 206. The court below and Sierra have recognized that these provisions of the Power Act are virtually identical with the comparable provisions of the Gas Act involved in *Mobile* (Sections 4(d), 4(e) and 5) and that, despite their slightly different postures, the basic issues in both cases are the same. And since the court below adopted the authorities and theory set out by the Third Circuit in *Mobile* in reaching its conclusion, the discussion in our briefs in No. 31 is fully applicable here and the Court is respectfully referred thereto.

B. While in *Mobile* the Third Circuit felt that the filed rate procedure was inequitable because it resulted in a "squeeze" on Mobile during the pendency of the hearing, there is no such possible inequity to Sierra. Sierra has benefited from this procedure because the

---

[12] Since in a hearing under Section 206(a) the Commission may fix only a prospective rate, "to be thereafter observed," the effect of the decision below is to nullify the challenged rate increase, to reinstate the 1948 rate, and in effect to require the excess over the 1948 rate collected by PG&E to be paid over to Sierra.

new rate was suspended for five months and then went into effect subject to refund. In contrast, the decision below would place a far greater burden upon PG&E, for under it the existing rate would continue in effect until the Commission finds in a new proceeding instituted under Section 206 that the existing rate is unreasonable, and this without any recourse by PG&E against Sierra for the difference in rates during the entire period of both administrative proceedings.

II

As an alternative ground for supporting the judgment below, Sierra has indicated that it intends to press its claim that the Commission's finding, that the new rate is reasonable, is not supported by substantial evidence. The District of Columbia Circuit, as we read its opinion, has recognized that the Commission's finding is amply supported and we discuss Sierra's contention only on the assumption that this Court may nevertheless wish to consider the question.

A. In passing on the reasonableness of the new rate proposed by PG&E—as is concededly proper under the filed rate procedure—the Commission utilized the cost of service test which it usually follows in rate proceedings, whether under Section 205(e) or Section 206. Finding that the new rate would provide a 4.75% return on a net investment rate base allocable to the service and that this was "not more than a fair return"—5½%—the Commission concluded that the rate was not unreasonable or unlawful. The propriety of the use of such cost of service method is well established, as is the propriety of allocating costs to assure that each customer bears its fair share of the overall costs of the utility's operations.

In addition, while Sierra could not, and did not, complain that the rate was too low, the Commission went on to consider the fact that the 4.75% return would be less than fully compensatory to PG&E. In view of the circumstances, particularly PG&E's willingness to accept the rate and its need to retain the Sierra business, the Commission concluded that the rate was reasonable. The allowance of a rate proposed by a utility which is less than fully compensatory accords with precedent.

B. The Commission rejected Sierra's claim that the usual cost of service method is irrelevant here because of the alleged circumstances under which Sierra entered into the 1948 contract with PG&E. Not only do the considerations which underlie the subjecting of contract and other types of rates to change by the same procedures strongly support the application of the same standards in passing on the reasonableness of the proposed rate changes, but the Commission found "unconvincing" Sierra's argument that in 1948 it had contracted with PG&E and foregone other sources of supply in reliance upon continuance of the low contract rates. The record shows that Sierra at that time considered PG&E to be the only feasible source and the alternative, the U. S. Bureau of Reclamation, to be objectionable in many ways.

Similarly, the Commission rejected Sierra's contention that the cost of service test should not be used because in 1948 PG&E took into account only the "incremental" cost of serving Sierra. Moreover, the Commission found that if the foreseeable rate of return from the contract rate when it was negotiated were to be accepted as the continuing reasonable return,

the new rate would do no more than restore the rate of return foreseeable in 1948.

Acceptance of Sierra's contentions would result in favored treatment for it. In contrast to the contracts of all PG&E's other customers at equivalent low rates which expire in 1955 and 1956, Sierra's contract has until at least 1964 to run and, should it be given continued effect, would operate to relieve Sierra for at least eight more years from paying its full share of the substantial and unexpected increases in PG&E's costs. It would be unfair thus to allocate the burden of these increased costs among PG&E's customers according to the existence of contracts and the order in which the contracts expire.

ARGUMENT

I

The Commission Properly Applied the Filed Rate Procedure Set Out in Sections 205(d) and 205(e) of the Power Act to the New Schedule Filed by the Public Utility, Even Though the Existing Rate Was Embodied in a Contract

A. *The Commission's Application of Sections 205(d) and 205(e) Accords With the Terms of the Power Act and the Usual Provisions of Utility Regulatory Statutes.*

When PG&E filed with the Commission a new rate schedule for the sale to Sierra, the Commission followed the filed rate procedure which has been long established and which it believes is mandatory under Sections 205(d) and 205(e) of the Federal Power Act, *infra*, pp. 39-41. Since the Commission's preliminary inquiry indicated that the newly filed rate might be unlawful, a hearing was ordered on the reasonableness of the new rate. Pending the outcome of that hearing, the Com-

mission suspended the rate for the maximum period allowed by the Act, and when that period expired before the hearing was terminated, and the increased rate went into effect in accordance with Section 205(e), the Commission directed that the difference be held by PG&E, with the excess over a reasonable rate (as ultimately determined by the Commission) subject to refund. After the hearing, the Commission found that the new rate was reasonable and terminated the proceeding.

Since the existing rate superseded by the new schedule thus approved by the Commission had been embodied in a contract between PG&E and Sierra, and Sierra had not agreed to the increase, the court below held that the Commission erred in following the filed rate procedure and should instead have applied the procedure provided in Section 206(a) of the Power Act. While it recognized that "[i]n modifying a filed rate under §205, it is not necessary to prove that the original rate is unjust or unreasonable; the new rate will take effect if the utility sustains the burden of proving that it is 'just and reasonable'." (R. 480), the court below ruled that where the existing rate is embodied in a contract it may not be changed in the absence of a finding, under the complaint hearing procedure provided in Section 206(a), that the existing rate is unreasonable (R. 480-481).

Noting that the Third Circuit's decision in *Mobile Gas Service Corp. v. Federal Power Commission*, 215 F. 2d 883, [now pending on writs of certiorari Nos. 17, 31, this Term,] involved the same issue, *i.e.*, whether the commission may "abrogate a pre-existing contract without any finding that the contract rate was unreasonable" (R. 481), and that the language of Sections 4 and

5(a) of the Natural Gas Act involved in *Mobile*, "corresponds almost verbatim" with Sections 205 and 206(a) of the Power Act (R. 481; see also R. 482, fn. 16),[13] the court below held fully applicable here the grounds relied upon by the Third Circuit (R. 481-482):

> * * * (1) cases arising under the Public Utility Law of Kansas which contained provisions similar to §§ 4 and 5(a) of the Natural Gas Act; (2) the interpretation of the Gas Act adopted by the Court of Appeals for the Tenth Circuit in Colorado Interstate Gas Co. v. Federal Power Comm.; (3) the doctrine that common law rights will not be impaired without a clear authorization; (4) a colloquy at hearings on a predecessor bill; and (5) the significant lack of debate on the question in view of the drastic impact wholesale abrogation of contracts would have had on the natural gas industry. * * *.

The Commission's brief in No. 31 points out in detail the invalidity both of the Third Circuit's ruling and of the grounds upon which it is based. Since the court below relied on the same grounds in reaching its con-

[13] Sierra has also conceded that "so far as the basic issue involved is concerned, the two (Power and Gas) Acts are so substantially identical that a decision by this Court in one would necessarily be controlling in the other" (Resp. Br. in Answer in No. 51, p. 2; see also Resp. Br. in Answer in No. 53, p. 1). However, it has been suggested that since Section 206(a) does not spell out, as explicitly as Section 5(a) of the Gas Act, the persons who may invoke the complaint procedure, a selling utility, unlike a selling gas company, may seek a rate change under Section 206(a). See Brief for Petitioner in No. 17, pp. 23, 80-81. However, as we have shown in our brief in *Mobile* (No. 31, p. 23, fn. 11; 36), Section 206(a) has the same effect as Section 5(a) of the Gas Act and the Commission has consistently so construed Section 206(a).

clusion, the discussion in our brief in No. 31 serves also as an answer here and we respectfully refer the Court to that brief for a detailed explanation of the Commission's position.[14]

In brief summary—as shown more fully in No. 31 (at pp. 23-24 and fns. 11, 12)—the filed rate procedure set out in Sections 205(d) and 205(e) is the only method available under the plain terms of the Power Act to a utility seeking to change its rate. The utility must initiate such changes by filing new schedules under Section 205(d); the Section 206(a) procedure may be invoked only by the Commission on its own motion or by complaint of someone other than the selling utility. This is so even where the existing rate is embodied in a contract, for it is the almost universal rule that contract rates are treated the same as other rates and the terms of the Power Act preclude any distinction between them. See Commission's Brief in No. 31, pp. 25-35. The Commission, in its application of the filed rate procedure and its regulations, has consistently treated rates embodied in contracts in the same manner

[14] The identity of the issues is not affected by the different posture of the two cases. While in *Mobile* the use of the filed rate procedure to alter contract rates was challenged at the outset, before hearing and order, Sierra attacked a Commission order which found the proposed rate reasonable, after a proceeding under the filed rate procedure. The same statutory question is raised in both cases since if the filed rate procedure is properly invoked the Commission could enter into a hearing solely directed to the reasonableness of the proposed rate. See *supra*, pp. 4, 14; *infra*, p. 22, fn. 19. Both the decision in the instant case and *Mobile* were based on statutory grounds and raised no constitutional question, as pointed out in the Commission's Brief in No. 31, p. 25, fn. 13. The instant case is squarely covered by the holding on the constitutional issue in *Midland Realty Co.* v. *Kansas City Power & Light Co.*, 300 U.S. 109, 114, that the power to fix rates is not dependent upon or conditioned by "specific adjudication in respect of existing contract rates."

as other rates. See R. 458-60; Commission's Brief in No. 31, pp. 35-40. Contracts are not thereby, "abrogated", as feared by the court below (R. 479, 481) and the Third Circuit (No. 34, R. 148), but are merely made subject to change as is customary with utility contracts in accordance with the methods prescribed by Congress (Commission's Brief in No. 31, pp. 31-33). Consequently, "the doctrine that common law rights will not be impaired without a clear authorization" (R. 481) has no part here.

The Court of Appeals believed that the Commission's construction would have "drastic" results (R. 482), thus following the lead of the Third Circuit, which considered it of a "radical nature" (No. 31, R. 154; Commission's Brief in No. 31, p. 44). But, as we have shown in No. 31, these characterizations are without justification. The legislative history, although meager, indicates that Congress did not intend to differentiate between contract rates and others so far as the applicable procedure is concerned.[16] Moreover, the Commission's reading of the filed rate provisions accords with the accepted construction of the comparable provisions

[15] The Commission's regulations governing the filing of rates and changes in rates under the Power Act, 18 CFR 35.1-.13, are in this respect to the same effect as the regulations under the Gas Act described in the Commission's Brief in No. 31, pp. 35-40.

[16] While the legislative history of the Power Act, like that of the Gas Act discussed in the Commission's Brief in No. 31, pp. 40-54, does not treat specifically with the present problem, the committee reports on the Power Act, as those on the Gas Act (No. 31, pp. 41-42), describe the filed rate procedure as a method of changing rates applicable to *all* rates of the utility. H. Rep. No. 1318, 74th Cong., 1st Sess., p. 29; S. Rep. No. 621, 74th Cong., 1st Sess., p. 51. In contrast, the colloquy on a predecessor bill to the Gas Act (R. 481-2), was not addressed to the filed rate procedure and so has no bearing on the present problem. See Commission's Brief in No. 31, pp. 42-44.

of the Interstate Commerce Act, upon which the Power and Gas Acts' procedures were modeled (Commission's Brief in No. 31, pp. 46-55),[17] and also with the similar interpretations of analogous provisions of the overwhelming majority of state public utility regulatory statutes (Commission's Brief in No. 31, pp. 55-71). And this Court, and the state courts with but little dissent, have held that these filed rate procedures may be invoked by utilities to effectuate a change in rates fixed by contract. *E. g., Midland Realty Co. v. Kansas City Power & Light Co.*, 300 U. S. 109, affirming 338 Mo. 1141; *Menasha W. W. Co. v. Minneapolis, St. P. & S. S. M. Co.*, 245 U. S. 633, affirming 159 Wisc. 130; *Suburban Water Co. v. Oakmont Borough*, 268 Pa. 243, 248-250; *Public Service Commission v. Pavilion Natural Gas Co.*, 232 N. Y. 146, 150-51; *Harrison Electric Co. v. Citizens' Ice & Storage Co.*, 147 Ark. 502, 506-07; see also, *Armour Packing Co. v. United States*, 209 U. S. 56.

Accepting the views of the Third Circuit in *Mobile*, the court below refused to follow *Midland* because it was based on the Missouri court's construction of its statute (R. 482), but chose instead to follow *Wichita RR. v. Public Utilities Commission*, 260 U. S. 48, and other cases arising under Kansas law on the ground that they concerned "a comparable requirement in a Kansas statute" (R. 481). However, as is shown in the Commission's Brief in No. 31 at pp. 72-80, Missouri has the usual filed rate procedure corresponding to the Commerce, Power and Gas Acts and is typical of the usual procedure adopted by most states, whereas the Kansas

[17] The similarity between the Power and Gas Acts and their derivation from the Commerce Act are evident from the Acts themselves and have been recognized by Congress and the courts. See Commission's Brief in No. 31, pp. 44-47 and fn. 30, p. 46.

procedure differs materially from the usual filed rate procedure and reflects a minority deviation adopted in relatively few states.[18]

B. *The Application of the Filed Rate Procedure Does Not Result in Inequity to Sierra.*

In *Mobile*, the Third Circuit apparently was influenced in reaching its result by the feeling that since Section 4(e) of the Gas Act expressly prohibited suspension of new rates for industrial resales, such as were there involved, Mobile would be "squeezed" between the new rate for the gas it purchased from United and the lower rate at which it had contracted to sell the gas to the industrial users, and consequently that the application of that procedure would be inequitable to Mobile. The Commission's brief in *Mobile* (at pp. 81-89) shows, however, that this inequity may have been more apparent than real; the way may well have been open for Mobile to seek a higher rate for its resale. In any case, in view of the Third Circuit's recognition that the Commission had authority under the Gas Act to order a higher rate than that embodied in a contract (No. 31, R. 142, 146-8), whatever loss Mobile suffered was limited to the period of the Commission's investigation. Such losses constitute a necessary incident to rate investigations (*Hope Natural Gas Co. v. Federal Power Commission*, 196 F. 2d 803, 809 (C. A. 4)), and its failing upon Mobile rather than upon United was the result of

[18] The Tenth Circuit decision in *Colorado Interstate Gas Co. v. Federal Power Commission* (R. 481) is irrelevant since that case involved a proceeding under the hearing procedure of Section 5(a) of the Gas Act and the Tenth Circuit did not purport to pass on or express an opinion on the scope or applicability of the filed rate procedure of Section 4. See Commission's Brief in No. 31, pp. 98-99.

deliberate determination by Congress in allocating these unavoidable losses—that, while the selling gas company should generally bear the losses, in the single case where the proposed rate is for industrial resale the burden should be on the purchaser.

In the present case, the use of the filed rate procedure results in no possible inequity to Sierra. Not only does Section 205(e) fail to contain a prohibition against suspension of rates for industrial resale, comparable to that in Section 4(e) of the Gas Act, but the rates here involved were not for such sales. PG&E's proposed rate was suspendible under Section 205(e), and the Commission, in setting PG&E's new schedule down for hearing, suspended it for the full five month period provided by that Section. In addition, although the new rate went into effect when the suspension period expired before the Commission completed its investigation, this was subject to Sierra's right, also provided in Section 205(e), to receive a refund of the excess, if any, over the reasonable rate as ultimately determined by the Commission. *Supra*, pp. 4-5. Thus, Sierra was protected all during the rate investigation from paying any rate other than a reasonable one, and although the Commission found, as a result of its hearing, that the new rate filed by PG&E was reasonable, Sierra was relieved under the statutory scheme from paying that increased rate during the period it was suspended. *See Hope Natural Gas Co. v. Federal Power Commission*, 196 F. 2d 803 (C. A. 4).

By thus keeping the old rate in effect during the suspension period, the filed rate procedure operated, on the one hand, to benefit Sierra and on the other, to bur-

den PG&E with the loss suffered during the suspension period. In contrast, the result below would impose a far greater burden upon PG&E for under Section 206(a), which the court below held applicable (R. 480-2), the existing rate continues in effect until the Commission fixes a new rate "to be thereafter observed and in force," with no recourse against the purchaser should the Commission find as reasonable a rate higher than the existing rate. Indeed, the court below, by modifying its opinion, has imposed an even greater burden upon PG&E. By requiring the Commission to dismiss the case and to start anew under Section 206(a)—rather than permitting it to hold the Section 206(a) proceeding in the same case (the course sanctioned in its original opinion) (R. 482, 495)—the court below has in effect held that, even if the Commission in the new Section 206(a) proceeding should fix the rate at the increased level originally proposed by PG&E, PG&E is not entitled to any part of the increase not only for the period that the Section 206(a) proceeding will be before the Commission but also for the two year period that the Commission was erroneously, according to the court, considering the rate increase under Section 205(e). See *supra*, pp. 9-10, fn. 12.

II

The Commission's Determination That the Proposed Rate Filed by the Public Utility Was Reasonable Is Supported by Substantial Evidence

Sierra has indicated that if, contrary to the holding below, the Commission properly applied the filed rate procedure and directed the hearing held in the course

thereof to the reasonableness of the new rate,"[9] it intends to urge that the judgment is sustainable on the further ground that "the Commission's finding that the proposed new rate was lawful in the light of the circumstances surrounding the negotiations of the contract was arbitrary, capricious and contrary to the evidence" (Resp. Br. in Answer in No. 51, pp. 3-4).

While, according to Sierra, the court below did not reach this question (*ibid*), we believe that a fair reading of the opinion below reveals an implicit recognition by the court that the proposed rate, which would yield PG&E a 4.75% return rather than the 5½% return to which it concededly is entitled (R. 21), was reasonable. The court entered its judgment despite this recognition because it thought that, inasmuch as "statutory reasonableness is * * * represented by an area rather than a pinpoint," (*Montana-Dakota Utilities Co. v. Northwestern Public Service Co.*, 341 U. S. 246, 251), the Commission in a proceeding under Section 206(a) might also find the contract rate to be reasonable (see R. 480-481). In these circumstances, since the finding of the new rate's reasonableness was upheld by the court below, there is no occasion for this Court to go into this additional issue which Sierra intends to raise. See

---

[9] Section 205(e) is explicit in its provision that the hearing had by the Commission in following the filed rate procedure is directed to the reasonableness of the *new* rate. This the court below fully recognized (R. 480):

> In modifying a filed rate under § 205, it is not necessary to prove that the original rate is unjust or unreasonable; the new rate will take effect if the utility sustains the burden of proving that it is "just and reasonable."

See also, the similar recognition by the Third Circuit in *Mobile*, 28 (J), R. 143.

Universal Camera Corp. v. National Labor Relations Board, 340 U. S. 474, 491.[20] On the assumption, however, that the Court might agree with Sierra's reading of the opinion below and might be willing to pass on this issue without the benefit of the further views of the court below, we turn to this question.

A. *Applying Appropriate Standards for Fixing Rates, the Commission Properly Found that the Proposed Rate Will Provide No More than a Fair Return to the Public Utility from its Service to Sierra and Is Therefore Reasonable.*

In passing on the reasonableness of the new rate proposed by PG&E—which both the court below (R. 480) and the Third Circuit in *Mobile* (No. 31—R. 143) recognized as proper where the filed rate procedure is applicable—the Commission utilized the cost of service test which it usually followed in rate proceedings under both Section 206(a) (the complaint-and-hearing procedure) and Section 205(e) (the filed rate procedure). The Commission found (R. 469):

> 8. The increased rate embodied in Supplement No. 1 to Rate Schedule FPC No. 3 has been satisfactorily shown to be such as to provide not more than a fair return on the portion of PG&E's net investment rate base properly allocable to that service after proper allowance for all operating expenses, as shown by Exhibit 19.

[20] Whether on the record as a whole there is substantial evidence to support agency findings is a question which Congress has placed in the keeping of the Courts of Appeals. This Court will intervene only in what ought to be the rare instance where the standard appears to have been misapprehended or grossly misapplied.

Exhibit 19 (R. 295-298), upon which this finding is thus based, consists of a computation of PG&E's cost of serving Sierra upon the basis of operations during the test year 1952. Operating expenses and the investment rate base upon which a return is allowed (original cost less the accrued depreciation plus working capital) are allocated between the service to Sierra and to other customers in a manner consistent with applicable Commission precedents. The Exhibit incorporates changes proposed by the Commission's staff in the methods of computing cost of service and rate of return suggested by PG&E (R. 449, n. 5). The computation shows that the proposed rate would yield 4.75%, as compared to the 2.60% return under the existing rate (R. 295). Since it was agreed by the parties that 5½% is a reasonable return for PG&E's electrical utility business on a net investment rate base (R. 21),[21] a comparison of this agreed reasonable return with the 4.75% return from the new rate leaves no doubt that, at least as far as Sierra is concerned, the Commission was justified in finding the new rate reasonable.[22]

While PG&E itself had proposed the new rate and no contention was made by Sierra that it was unreasonably low (indeed, Sierra seeks to keep it lower, see *infra*, p. 27*ff*); the Commission was careful to con-

[21] It was also stipulated that a duly qualified Commission witness would testify that the method employed in Exhibit 19, which showed that the new rate would provide only 4.75%, was reasonable and proper (R. 63). Both stipulations were made without prejudice to Sierra's right to claim that the stipulated facts were "not relevant or material" (R. 21; 63).

[22] In contrast, the Commission noted that (R. 464) "if a finding on the lawfulness of the 1948 contract rate were necessary or appropriate, on the record before us that finding would have to be that the 1948 rate is unreasonably low and therefore unlawful."

sider the question of the deficiency in the rate of return which the new rate will produce." It found that the 4.75% return, although less than fully compensatory, was a reasonable rate of return for this particular part of PG&E's electric department's business because (1) PG&E had regarded that reduction from the 5% rate of return as warranted to attract and retain this business and (2) "[w]ith the investment which PG&E has made and has undertaken to make in special facilities on which it would earn no return at all if it lost this particular business, it would require evidence of a kind not presented in this record to warrant a finding that the 4.75% rate of return it is willing to accept from this sale is unreasonably low" (R. 465). The Commission pointed out, however, that "no such considerations, on this record, warrant a conclusion that any rate substantially lower than that proposed would be reasonable." (R. 466). In the light of this need by PG&E to retain the Sierra business and its willingness to accept a less than fully compensatory rate, plus the fact that any deficiency would not be borne by other customers and that no undue discrimination or preference would result, the Commission concluded (R. 469):

> 9. No other facts have been shown affecting the justness and reasonableness of the proposed rate, and it is therefore not unjust or unreasonable.

The Commission also found that the new rate was not unduly discriminatory when compared with other PG&E rates (Fdgs. 10 and 11, R. 469-470) and accordingly concluded that the rate was not unlawful. (Fdg. 12, R. 470).

Thus, the Commission made all of the determinations and used the criteria which were clearly appropriate and proper under well-established principles of utility rate regulation. The propriety of the use of such cost of service, based upon the prudent investment rate base, is well established. *Federal Power Commission v. Hope Natural Gas Co.*, 320 U.S. 591; *Colorado Interstate Gas Co. v. Federal Power Commission*, 324 U.S. 581; *Panhandle Eastern Pipe Line Co. v. Federal Power Commission*, 324 U.S. 635; *Cities Service Gas Co. v. Federal Power Commission*, 155 F. 2d 694 (C.A. 10), certiorari denied, 329 U.S. 773; *Safe Harbor Water Power Corp. v. Federal Power Commission*, 179 F. 2d 179, 196-201 (C.A. 3), certiorari denied, 339 U.S. 957; *Pennsylvania Water & Power Co. v. Federal Power Commission*, 193 F. 2d 230, 241-246 (C.A.D.C.), affirmed, 343 U.S. 414, 417. Also firmly settled is the propriety of so allocating costs as to assure that each portion of the utility's business bears its fair share of the overall cost of the utility's operations. *Colorado Interstate Gas Co. v. Federal Power Commission*, 324 U.S. 581, 586-595; *Northern Pacific Ry. v. North Dakota*, 236 U.S. 585, 594, 596-597; *Banton v. Belt Line Ry.*, 268 U.S. 413, 419-422. The Commission's refusal to disturb PG&E's managerial discretion in proposing a less than fully compensatory rate likewise accords with precedent. *Interstate Commerce Commission v. Chicago Great Western Ry.*, 209 U.S. 108, 118-119.

It is, of course, the function of the Commission "to reduce the abstract concept of reasonableness to concrete expression in dollars and cents." *Montana-Dakota Co. v. Public Service Co.*, 341 U.S. 246, 251.

Since the proposed rate imposes upon Sierra no more than its fair share of providing a reasonable return to PG&E, the Commission's approval of the rate is fully justified. As the Court pointed out in *Federal Power Commission v. Hope Natural Gas Co.*, 320 U.S. 591, 602, "It is not theory but the impact of the rate order which counts. If the total effect of the rate order cannot be said to be unjust and unreasonable, judicial inquiry under the Act is at an end." See also *Federal Power Commission v. Natural Gas Pipeline Co.*, 315 U.S. 575, 586.

B. *The Commission Was Not Required to Depart from the Established Rate-Making Standards by Sierra's Claim of Special Circumstances Surrounding Negotiation of the 1948 Contract Rate.*

As already indicated, Sierra does not claim that the proposed rates are unreasonably low, but rather that the rate should be even lower, *i.e.*, at the level provided in the 1948 contract. Sierra claims that the usual cost of service method of determining reasonableness of rates is irrelevant here, and that a different method should be followed because of the circumstances under which it entered into the 1948 contract with PG&E. (R. 432, 450, Sierra Rev. 7, 9-10). According to Sierra, it entered into the 1948 contract in reliance upon the lower contract rates and thereby gave up the opportunity to obtain cheap power from other sources, notably from the United States Bureau of Reclamation; and it declares that PG&E offered the contract rate in order to retain Sierra's business, with the expectation that it would cover the incremental cost of the service rather than yield any specific rate of re-

supra, R. 150-154; Pet. Rev. 7-10).[28] The Commission, however, disagreed with Sierra's version of the IPFs circumstances and, in any event, concluded that, even if that version were well founded, it would not constitute sufficient reason for departing from the cost-of-service test.

1. Existence of a Contract Does Not Alter the Test of Reasonableness. The very considerations which prompt legislatures to subject changes in contract rates to the same procedures as changes in other rates strongly support the application of the same set of standards for passing on these rate changes. As we pointed out in No. 31 (at pp. 26-27), the fact that an existing rate is fixed by private contract has little, if any, bearing on the reasonableness of the proposed change, or, for that matter, of the contract rate itself. For in agreeing upon the rate, the parties are motivated primarily by purely private considerations without regard to reasonableness, as such, whereas the Commission considers the reasonableness of rates in light of an entirely different set of criteria, such as the relationship of the rate to, and its impact upon, the rest of the utility's rate structure. For this reason, not only are contract rates almost universally subject to change in the same manner as non-contract rates, but the same criteria have been utilized in passing upon proposed changes. (*Duquesne Light Co. v. Public Service Commission*,

[28] Sierra also contended that because the 1948 contract rate was negotiated under competitive conditions, it necessarily remained just and reasonable, that it would be unfair to change the rate in the 1948 contract while leaving all its other terms unaltered, and that its position was supported by rulings of the California Commission. See R. 450-452; *supra*, pp. 6-8.

273 Pa. 287, 294-295, 298.[2] While unvarying utilization of the cost of service test has been questioned, any proposed modification has been based on public utility principles and the nature of the regulated industry, not on the presence or absence of private rate contracts. See *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U.S. at 601-605, 647-652. Similarly, while this Court has permitted non-compensatory rates on one portion of a utility's business, this also has been based upon special considerations in the public interest, not upon the existence *vel non* of private agreements. *B. & O. R.R. Co.* v. *United States*, 345 U.S. 146, 148-150.

2. *The facts, as found by the Commission, did not justify departure from the cost of service test.* (a). The Commission found "unconvincing" Sierra's argument that it had contracted with PG&E and foregone other sources of supply in reliance upon continuance of the low contract rates (R. 451). Of course, Sierra could never have expected that the rates would con-

[2] The court there noted that it was error "to restore to appellants the contract rates, without determining or even considering whether [the existing schedules] would yield to the two companies the fair return to which they were entitled * * *" (273 Pa. at 294-295), and then observed (273 Pa. at 298): "* * * if the contracts are to be held binding under all circumstances, as at one time appeared to be appellant's claim, then the statute but slightly changes the preexisting law, so far as concerns this matter, and the scandals growing out of favored terms being given to friends of the management will be received, although it was the intent of the Public Service Company Law to cut up by the roots all such possibilities. On the other hand, if the contracts, without other evidence, are to be so construed as to compel appellees to give to appellants a preferential rate by putting the latter in a class by themselves, as appears later to have been contended, not only are they thus given a great advantage over other large consumers (though the contracts themselves do not give it), but the foregoing objection will still remain, though slightly modified in form."

time during the contract term regardless of circumstances, since it has always conceded that the rate could be changed by order of the regulatory agency (R. 54, 145, 329, 458, Pet. Rev. 5-6). Moreover, even if Sierra's reasons for entering the contract were relevant (but see *supra*, pp. 28-29), the record supports the Commission's conclusion that in 1948 Sierra considered PG&E the only feasible source.

Sierra at that time sought a dependable source of power which would be available when the limit of the capacity of the existing transmission lines was reached in 1949 (R. 6-8, 32-33, 170-171, 199-200, 205-208, 231-232, 264) and PG&E was the only source which could be ready to supply it at that time (R. 15-16, 32, 203, 221, 264, 353). The one alternative seriously considered by Sierra was Shasta Dam power from the U.S. Bureau of Reclamation, which tendered a proposed contract.[25] However, the Bureau would not have completed its first transmission line before 1951 or 1952, and even this date was conditioned upon appropriations by Congress (R. 16, 32, 211, 222, 231, 347-348, 350, 353).

Sierra's contemporaneous memoranda and statements indicate other objections, including that until 1956 the Bureau would provide only a single-long transmission line which was unreliable because of the hazards of interruption (R. 209, 222-227, 351, 353-354); the Bureau service was entirely contingent on Shasta's

[25] According to statements in the record, Sierra also considered obtaining the additional power from California Electric Company, Idaho Power Company, and through an expansion of its own power plants (R. 23, 205, 218). However, the record contains only a brief discussion of the possibilities of power from California Electric Company (R. 42-47), and Sierra's own development (R. 47-50, 217, 221) and there is no indication of any earnest exploration by Sierra of any of these alternatives.

water supply, with no diversified sources of power (R. 210, 223-224, 230, 351, 354); other arrangements for standby power would have been required (R. 222, 224, 229-230, 304, 347-348, 351, 353-354); and Sierra was not favorable to the expansion of public power (R. 173, 347). In general, Sierra officials contemporaneously characterized the Bureau's proposal as "highly speculative" (R. 234, 252), "premature and objectionable in many ways" (R. 355, 223), and believed that PG&E offered the "best and most dependable contract" (R. 206, 216) and the "best source of supply" available (R. 223, 209-210, 226, 351).

Sierra, it is true, did seek low contract rates from PG&E (R. 174-176). In January 1947, PG&E offered Sierra a 15-year contract at the then existing rates (R. 182-185) and only thereafter, in December 1947, agreed to the lower rates to be embodied in the 1948 contract (R. 340-342). However, it is evident that PG&E's rate was not the decisive factor leading Sierra to the contract since Sierra did not know, when it contracted with PG&E, how much the Bureau of Reclamation power would cost it. While the rate offered by the Bureau was .555 mills less than the PG&E rate (R. 33, 221), this Bureau rate did not include the necessary standby arrangement nor the cost to Sierra of the additional facilities for connecting transmission lines and stepping down voltage (R. 39, 224, 229).[26] And for these reasons

[26] Some idea of the probable cost of firming up the 90,000 kw which would be contracted for with the Bureau is afforded by the fact that Sierra paid $30,000 to PG&E to firm up 4,000 kw of power supplied from its own hydroelectric plants under the 1938 contract rate (R. 140-141). The cost to Sierra of special facilities under the Bureau transaction may be indicated by Sierra's anticipated expenditure of $750,000 for such special facilities when PG&E's first additional transmission line was constructed (R. 207).

Sierra's management realized at the time that it was not clear whether the cost of Bureau power would be more or less than PG&E power (R. 351, 355). Sierra's water resource engineer stated that they "didn't progress far enough" with the Bureau's proposal "to enter into those details" which would determine the actual cost to Sierra of Bureau power (R. 39). In 1948, when asked before the California Commission about possible additional charges by the Bureau for standby power, he testified, "It did not seem worth while trying to talk that over * * * because the balance of the contract did not seem to justify its acceptance." (R. 224.) [27]

(b). The Commission similarly rejected Sierra's effort to get the benefit of the 1948 contract rate through its argument that the criterion upon which it claims PG&E based its decision to execute that contract must be applied to test the reasonableness of any new rate. That criterion, according to Sierra, was the sufficiency of the rate to compensate PG&E for its incremental cost of serving Sierra, in addition to all other customers at the same level of service, rather than the average cost of service at that level.

---

[27] The contract offered by the Bureau is in the record (R. 309-24) and it manifestly contains numerous features troublesome to Sierra: the Colorado River Commission (the contracting party for resale to Sierra) would be required to give priority to public agencies and cooperatives (R. 313); the United States would be under no obligation to furnish power until its facilities were ready, as conclusively determined by the contracting officer (R. 321); there would be no obligation in case of the inadequacy of water to generate power (R. 322); and the contract and the liability of the United States would be contingent upon future congressional appropriations (R. 323). While it appeared to Sierra in February 1948 that, of the "numerous objections," "some * * * might be eliminated by negotiations" (R. 351), it is apparent that not all of them could be so eliminated.

In considering this contention, the Commission undertook an analysis of the situation as it existed in 1948 under the cost of service method, and ordered argument as to the future rate of return and future changes in capacity, sales, operating expenses and plant investment which were foreseen or reasonably foreseeable in 1948. (R. 438-39, 446-447.) Exhibit 35 (R. 356-408) was accordingly prepared by PG&E, utilizing estimates of sales, costs and capital that had been actually made and used by PG&E in 1946 and 1947 (R. 81-88, 92-96, 101-3, 365-66, 372, 392-94). From these basic data, it was possible to compute the rate of return which was reasonably foreseeable when the 1948 contract was consummated (R. 88-89, 132, 361).[28] And, comparing the foreseeable return from PG&E's proposed new rate (for the period beginning in 1952) with the prospects of return from the contract rate foreseeable in 1948, the Commission concluded: "* * * there is no substantial difference between the rate of return which PG&E seeks by the present proposal, and that which was reasonably foreseeable at the time the 1948 contract was negotiated." (R. 453.)

---

[28] In Exhibit 35, the reasonably foreseeable return is assumed to have been predicted in the third quarter of 1947, since from then on PG&E was committed to the contract rate (R. 392). The revenue and sales figures were actually used in a 1947 study, based on the then estimated demand (R. 365-6). Capital figures include an actual 1947 estimate of the cost of special facilities for Sierra and the units of investment in PG&E's system's network capital actually used in 1947, multiplied by Sierra's future demand as estimated in 1947 (R. 372). For unit costs, actual 1946 figures were the latest available when the contract was negotiated, but PG&E increased these by 10%, finding that such allowance might have been reasonably made in view of rising prices being then experienced (R. 384-5, 84-5). Since this 10% increase reduces the reasonably foreseeable return, it thus constitutes a concession by PG&E (R. 453, fn. 9).

Sierra objected to the Commission's concern with the rate of return reasonably foreseeable in 1948 under the contract, contending that this was purely hypothetical because no specific rate of return was actually foreseen by PG&E at that time (R. 453; Pet. Rev. 7). However, as the Commission's opinion pointed out, PG&E did have substantially equivalent information in 1948 upon which to compute its rate of return.[29] In any case, the Commission found that there was no reason for it to depart from its customary practice of allocating the cost of PG&E's service among Sierra and other customers, even if PG&E had struck the 1948 bargain on its view of the "incremental" cost of maintaining service to Sierra (R. 454-55).

As pointed out above, *supra*, pp. 23-26, the reasonableness of a rate for a particular service can be tested by comparing the revenues that rate will produce with the utility's cost of rendering that service, allocating costs applicable to more than one service upon an average basis, and using a reasonable rate of return on the prudent investment to determine capital costs. In weighing Sierra's plea for special equitable treatment the Commission was only willing to go so far as to consider what the effect would be if the foreseeable rate of

[29] The cost of service study used by PG&E at the time the contract was negotiated set out the unit cost per kilowatt-hour of the company's integrated system and the additional cost of the special facilities for Sierra's service, such costs including a 6% return. (R. 113-6). This did not follow the method of Exhibit 19 (*supra*, p. 24); it did not allocate a portion of PG&E's rate base to the Sierra service and then calculate a percentage return to be yielded by the revenues from the proposed rates (R. 114). However, since a comparison of unit revenues with PG&E's unit cost figure would show the estimated deficiency from a 6% return (R. 114, 116), PG&E did have, as the Commission noted, "substantially equivalent information." (R. 453).

return from the contract rates when the contract was negotiated were to be deemed the continuing reasonable return from the service to Sierra, *i.e.*, its fair share of the burden of providing a reasonable return to PG&E's system (R. 452). That requirement was fulfilled, since the new rate would do no more than restore the previously foreseeable rate of return.

3. *Sierra seeks favored treatment.* Examination of the record reveals that acceptance of Sierra's contentions would result in favored treatment for it. Besides Sierra, PG&E supplies power for resale to 13 other customers at rates lower than the proposed rate, most of these at rates equivalent to Sierra's 1948 contract rate (R. 411-12). Moreover, while Sierra's contract will extend at least to 1964,[30] all the other low rate resale contracts will expire by 1955, except that with the City of Alameda, which will expire in 1956 (R. 268-71, 283-4, 287, 411-3). PG&E's further resale contracts with 8 public utility corporations are at the rate which it has now proposed for Sierra (R. 412-13). In these circumstances, it is clear that in the near future all of the other low rate contracts will have expired, and Sierra alone, should its contentions be accepted, would be charged the low contract rate for an additional period of at least eight years. Sierra, alone, would thus be relieved from paying its allocable share of PG&E's increased costs, costs which have increased substantially and unexpectedly since the contract was entered into in 1948 (R. 92, 282, 285, 358, 399).

---

[30] The contract, by its terms, was to remain in effect until 1964 or 15 years from the date of entry into service of PG&E's additional line—or of a second line, if necessary—whichever is later. A second transmission has been found necessary and it is expected to go into service in 1956. Consequently, the contract will probably be operative until 1971.

While Sierra has sought to justify such favored treatment by reference to its version of the circumstances surrounding the negotiation of the 1948 contract and its asserted reliance thereon, the simple fact is that all PG&E's customers, whether under contract or not, similarly rely in purchasing power from PG&E and fixing their resale rates, on their assumptions of future costs of power, as well as on other cost and market factors. It would be unfair to allocate the burden of increased costs among PG&E's customers according to the existence of contracts and the order in which contracts expire. In utility regulation, benefits and losses are not fortuitous functions of varying dates and terms of contracts.

Sierra has sought support from a decision of the California Commission, the regulatory agency having jurisdiction over all the customers of PG&E, other than Sierra, who have been furnished power under low-rate contracts (R. 280-3, 411-3, 456-7, 469). In 1951, PG&E applied to the California Commission for an increase in its contract rates to them; Sierra's rates were also included since, until *United States* v. *Public Utilities Commission of California*, 345 U.S. 295, it was not deemed clear by PG&E that the Power Commission had exclusive jurisdiction over the sale to Sierra.[31] The

[31] PG&E could not obtain a rate increase without such application under California law, which differs from the Power and Gas Acts and most state statutes and does not contain the usual filed rate procedure. See Commission's Brief in No. 31, pp. 68-69. California Public Utilities Code, Sec. 454, provides: "No public utility shall raise any rate or so alter any classification, contract, practice, or rule as to result in any increase in any rate except upon a showing before the commission and a finding by the commission that such increase is justified." Section 455, the typical suspension and hearing section of the filed rate procedure, expressly does not apply to proposed increases in rates.

California Commission acceded to the purchasers' pleas on the equities and refused to order higher rates but gave the parties an opportunity to renegotiate the contracts in the light of the higher basic resale schedule (equivalent to Sierra's proposed new rate in the instant case) which it then authorized (R. 280-91). Of course, the Federal Power Commission is not bound by the attitude of the California agency on the equities. Moreover, all the rates subject to the California Commission's jurisdiction are imminently subject to renegotiation because of the expiration dates of the contracts. Only Sierra's contract would remain outstanding, and it would last for 8 to 16 more years. Consequently, acceptance of Sierra's contentions, even taking into consideration the special treatment which the California Commission was willing to accord to the rate contracts subject to its jurisdiction, would have the result of permitting Sierra's low contract rate, alone of all the contract rates involved, to control for a substantial additional period.

CONCLUSION

For the foregoing reasons, it is respectfully submitted that the judgment below should be reversed.

SIMON E. SOBELOFF,
Solicitor General.
WARREN E. BURGER,
Assistant Attorney General.
MELVIN RICHTER,
LIONEL KESTENBAUM,
Attorneys.

WILLARD W. GATCHELL,
General Counsel,
HOWARD E. WAHRENBROCK,
Assistant General Counsel,
WILLIAM J. GROVE,
Assistant General Counsel,
DREXEL D. JOURNEY,
Attorney,
Federal Power Commission.

SEPTEMBER, 1955.

APPENDIX

The Federal Power Act, 49 Stat. 838, 847; 16 U. S. C. 824, *et seq.*, provides in pertinent part:

SEC. 205. * * *

(c) Under such rules and regulations as the Commission may prescribe, every public utility shall file with the Commission, within such time and in such form as the Commission may designate, and shall keep open in convenient form and place for public inspection schedules showing all rates and charges for any transmission or sale subject to the jurisdiction of the Commission, and the classifications, practices, and regulations affecting such rates and charges, together with all contracts which in any manner affect or relate to such rates, charges, classifications, and services.

(d) Unless the Commission otherwise orders, no change shall be made by any public utility in any such rate, charge, classification, or service, or in any rule, regulation, or contract relating thereto, except after thirty days' notice to the Commission and to the public. Such notice shall be given by filing with the Commission and keeping open for public inspection new schedules stating plainly the change or changes to be made in the schedule or schedules then in force and the time when the change or changes will go into effect. The Commission, for good cause shown, may allow changes to take effect without requiring the thirty days' notice herein provided for by an order specifying the changes so to be made and the time when they shall take effect and the manner in which they shall be filed and published.

(c) Whenever any such new schedule is filed the Commission shall have authority, either upon complaint or upon its own initiative without complaint, at once, and, if it so orders, without answer or formal pleading by the public utility, but upon reasonable notice, to enter upon a hearing concerning the lawfulness of such rate, charge, classification, or service; and, pending such hearing and the decision thereon, the Commission, upon filing with such schedules and delivering to the public utility affected thereby a statement in writing of its reasons for such suspension, may suspend the operation of such schedule and defer the use of such rate, charge, classification, or service, but not for a longer period than five months beyond the time when it would otherwise go into effect; and after full hearings, either completed before or after the rate, charge, classification, or service goes into effect, the Commission may make such orders with reference thereto as would be proper in a proceeding initiated after it had become effective. If the proceeding has not been concluded and an order made at the expiration of such five months, the proposed change of rate, charge, classification, or service shall go into effect at the end of such period, but in case of a proposed increased rate or charge, the Commission may by order require the interested public utility or public utilities to keep accurate account in detail of all amounts received by reason of such increase, specifying by whom and in whose behalf such amounts are paid, and upon completion of the hearing and decision may by further order require such public utility or public utilities

to refund, with interest, to the persons in whose behalf such amounts were paid, such portion of such increased rates or charges as by its decision shall be found not justified. At any hearing involving a rate or charge sought to be increased, the burden of proof to show that the increased rate or charge is just and reasonable shall be upon the public utility, and the Commission shall give to the hearing and decision of such questions preference over other questions pending before it and decide the same as speedily as possible.

SEC. 206 (a) Whenever the Commission, after a hearing had upon its own motion or upon complaint, shall find that any rate, charge, or classification, demanded, observed, charged, or collected by any public utility for any transmission or sale subject to the jurisdiction of the Commission, or that any rule, regulation, practice, or contract affecting such rate, charge, or classification is unjust, unreasonable, unduly discriminatory or preferential, the Commission shall determine the just and reasonable rate, charge, classification, rule, regulation, practice, or contract to be thereafter observed and in force, and shall fix the same by order.

* * * * *

SEC. 306. Any person, State, municipality, or State commission complaining of anything done or omitted to be done by any licensee or public utility in contravention of the provisions of this Act may apply to the Commission by petition which shall briefly state the facts, whereupon a statement of

the complaint thus made shall be forwarded by the Commission to such licensee or public utility, who shall be called upon to satisfy the complaint or to answer the same in writing within a reasonable time to be specified by the Commission. * * *

☆ U. S. GOVERNMENT PRINTING OFFICE 1988 — 550-069 — 559